

FREE TRADE AGREEMENT - ECONOMIC IMPACT ON BILATERAL WHEAT TRADE

Discussion

Total annual global wheat production is normally approximately 600 million tonnes, with only approximately 100 million tonnes traded internationally. This highlights the fact that many countries currently meet most of their domestic needs, and the export trade is therefore more generally focused on supplying net importing markets such as Egypt, Brazil, Japan, China, Algeria, Iran, Indonesia, South Korea and EU.

Both Australia and the US are both significant producers and global net exporters of wheat, often jointly supplying more than 40% of the world's wheat trade. Given the high surplus production levels, the demands of the respective domestic markets are easily met in most years.

The latest published International Grain Council statistics indicate the US annually produces on average 64 million tonnes of wheat, with 30 million tonnes exported. Australia annually produces on average 18 million tonnes of wheat, with 14 million tonnes exported.

Australia has a deregulated domestic market, and producers have a choice to either sell directly into contracts or cash sales to flour millers or feed suppliers, or into the national co-operative export pool. This ensures the domestic market operates on a world parity price basis, and there can be no cross subsidisation between domestic and export markets, a fact reaffirmed by past detailed investigations by the General Accounting Office (GAO).

In most years there is sufficient wheat produced in Australia to easily meet domestic demand, particularly given the ability of feedgrain users to substitute alternative grains such as sorghum, corn, barley, oats and pulses. However in years of drought, such as 2002, overall grain shortages have created the opportunity for imports of wheat (ex UK) and corn (ex USA) to occur, and these have occurred without any market obstacles.

Current Barriers to Trade

Australia does not export wheat to the US because of:

- the inability of unsubsidised Australian export wheat to compete directly with generous Farm Bill concessions for US wheat producers,
- the significant impact of long distance freight costs,
- the traditionally high level of US production and reserves,
- the advantageous economic alternative in years of low supply for the US to source Canadian or EU wheat at a lower cost than Australian wheat.

There are currently no formal market barriers such as tariffs or quotas to inhibit bilateral wheat trade, however there are some less visible constraints such as the Jones Act which imposes extra costs on the shipping of Australian commodities to multiple US ports at times when it is cheaper to use foreign flag vessels.

There is currently no bilateral wheat trade between the US and Australia, however the Australian wheat industry recognises that in the future there may potentially be emerging niche markets in each country which cannot be met from within the current production quality spectrum, and there may be the potential opportunity for a low level of beneficial bilateral trade to occur on a regular basis.

Australian Co-operative Marketing Arrangements

Like the US, Australia supports co-operative principles for the collection and marketing of many of its primary commodities, and has encouraged such bodies to operate on a fully commercial basis to ensure no trade distortions can occur.

The Australian Wheat Board was formerly a government supported statutory authority which has now been fully commercialised. AWB Ltd is now a private co-operatively styled company whose capital shares can be openly traded on the Australian Stock Exchange. However more than 85% of the shares are still held by wheatgrowers, and the control of the company is permanently entrenched with wheatgrowers, regardless of capital shareholding.

The company is uniquely structured to ensure the National Pool is legally separate from all other company operations, and its performance is rigorously monitored independently by the Wheat Export Authority to ensure the company maximises net returns to growers. This is a legislative requirement of government on the company's operations, and one which is monitored very seriously by government.

As distinct from marketing bodies in other countries, the government provides no underwriting or guarantees, no direct or indirect financial support, and has no say whatsoever in any decision-making.

The wheatgrowing shareholders of AWB Ltd have set the company's number one Constitutional requirement as the need to maximise net returns to growers. Failure of the company to achieve this would be a breach of the company's legal obligations under Australian Corporations Law. The Constitution can only be changed by a 75% overall majority vote by wheatgrowers alone, as well as a majority in every one of the five wheatgrowing states. Australia's wheatgrowers will not tolerate any margin trading activities which would deliver less than the optimum price for their product.

In keeping with its legal obligations, the AWB National Pool is a not-for-profit co-operative entity which, after the deduction of marketing expenses, returns all premiums directly to wheatgrowers participating in the Pool.

Ability of AWB Ltd to attain market premiums

The Wheat Export Authority's 2002 report indicated AWB Ltd gains a premium of between US\$8-18 per tonne more than the price received for comparable grades elsewhere, supporting the fact that AWB does not, and legally cannot, undercut comparable US market sales.

AWB Ltd believes the commercial structure provides an excellent working model for US's 3000 co-operatives to adopt. The collective principles of marketing allow the segregation of all grain qualities to be maintained until the customers announce their exact specifications, and the tailored cargoes can then be assembled from the inventory.

This is a healthy new dimension to the whole grain production and marketing system, as it ensures the market receives exactly what it needs, particularly in the increasingly segmented and highly differentiated South East Asian markets, and encourages demand, confidence and investment throughout the marketing chain.

Comparison with US co-operative marketing

AWB Ltd has 40,000 growers in its co-operative body, while as an example, the State of Missouri has 109,000 farmers registered in co-operatives. Almost all of US's 2 million farmers are reported to be members of one or more of the 3000 co-operatives in operation nationally.

US co-operatives operate in a highly protected environment which delivers considerable concessions in the forms of taxation and other benefits which AWB Ltd does not enjoy.

Summary

Due to the net global exporting status of the two countries, the development of a Free Trade Agreement between Australia and the US is not likely to have any significant future impact on the current level of bilateral wheat trade.

The current co-operative marketing arrangements of AWB Ltd place upward pressure on global prices, thereby bringing positive economic benefits to US wheat producers.
